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IN THE

Supreme Court of the United States

OCTOBER TERM, A. D. 1942.

No. 516

EUNICE E. EASTMAN,
Petitioner,

vs.

GUARANTY TRUST COMPANY OF NEW YORK, ET AL.,
Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT AND BRIEF IN SUPPORT THEREOF.

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PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

To the Honorable, the Chief Justice and the Associate Justices of the Supreme Court of the United States:

Petitioner, Eunice E. Eastman, respectfully prays that a writ of *certiorari* issue to review the judgment of the United States Circuit Court of Appeals for the Second Circuit, entered in this cause on August 4, 1942, affirming the order of the District Court for the Southern District of New York sustaining respondents' motion for a summary judgment against the petitioner, plaintiff below.

Decisions Below. The decision of the District Court appears in the record at page 129 and is reported in 43 F. Sup. p. 37. The opinion of the Circuit Court of Appeals appears in the record at page 152 and is reported in 130 F. (2) p. 300.

Jurisdiction. The judgment of the Circuit Court of Appeals was entered August 4, 1942 (R. 152). Rehearing was denied on September 4, 1942 (R. 179). The jurisdiction of this Court is invoked under section 240 (a) of the Judicial Code, as Amended by the Act of February 13, 1925.

STATEMENT OF THE MATTER INVOLVED.

Nature of Proceedings. The United States Circuit Court of Appeals sustained respondents' motion for a summary judgment against the petitioner, the plaintiff below, on the ground that the respondent, Guaranty Trust Company of New York, the Trustee of a $30,000,000 note issue, owed no fiduciary duty to the petitioner, a holder of $10,000.00 of said notes, notwithstanding the acceptance of the trust duties by the Trustee, the issuance of the notes, and the sale of the $30,000,000 note issue to the public, including the petitioner, by a syndicate in which a wholly owned Subsidiary of the Trustee participated. The Court of Appeals held that petitioner was in no position to maintain the action for breach of trust against the Trustee because no trust relationship was established as there was no trust *res* in the Trustee's possession (R. 156). The court also held that even if any trust relationship existed, petitioner was not in position to recover as the profit realized by the Trustee was of doubtful value (R. 156). It resolved the doubt in favor of the movants, the respondents. One of the judges concurred in the decision on the latter ground (R. 157).

The Material Facts. Respondent, Guaranty Trust Company of New York, hereinafter called "Trustee", accepted its trust duties (R. 104) under a $30,000,000 note issue dated May 1, 1930 and maturing May 1, 1935, bearing interest at 6% per annum payable semi-annually, and issued by the Van Sweringen Corporation (hereinafter called "Company"). The Company was a wholly owned subsidiary of the Vaness Company (hereinafter called "Vaness"), whose principal officers, O. P. and M. J. Van Sweringen, owned 80% of its stock. The Company also owned the Cleveland Terminals Building Company, which will be referred to as "Subsidiary", (R. 18).

The Company covenanted by the terms of the trust indenture to keep $15,000,000 in "segregated assets" until one-half of the $30,000,000 note issue was paid off (R. 84). The Van Sweringen brothers agreed to supply "assigned securities" in order to maintain the "segregated assets" in liquid condition (R. 105-107). The Company was to hold in trust the "assigned securities" for the benefit of the noteholders (R. 86, 107), and covenanted not to pledge any of its assets under certain conditions (R. 82).

The Trustee affixed its corporate seal in evidence of its acceptance of the trusts thereby created (R. 104). The books and records of the Company were always to be open to the inspection of the Trustee (R. 89) and there were to be delivered to it statements of income and profit and loss annually (R. 90). The Company was required, on request of the Trustee, to furnish detailed information as to all of its acts and it agreed to execute further and additional instruments as may be required by the Trustee. The Trustee was vested with discretion to accelerate the entire $30,000,000 note issue in the event of default

(R. 92).* It had further discretion, subsequent to the acceleration, to waive the default and to rescind and annul the acceleration. The entire $30,000,000 was due to the Trustee on demand (R. 93) and the exclusive right of action was vested in it, including the right to file a claim in bankruptcy (R. 94). The Trustee was empowered to take any action to prevent any impairment of its rights and of the rights of the noteholders. The noteholders were prohibited from maintaining any suits in their own name (R. 96), and in order to require the Trustee to take any action, a demand was necessary by 25% of the outstanding notes conditional upon a tender of indemnity to the Trustee (R. 97). The Trustee was to receive compensation and was given a lien on all of the property for the payment of its fees (R. 101).

The respondents, the Trustee and Morgan, became creditors of the Company's Subsidiary to the extent of $11,000,000 each as participants in a $23,500,000 loan which was made in October, 1930 (R. 19). From such loan there was paid the first semi-annual interest on the $30,000,000 note issue (R. 18-20). Morgan held as collateral for itself and for the Trustee all of the common stock of the Company under the $23,500,000 note of the Cleveland Terminals Building Company (R. 21).

The assets of the Company consisted of its investment in its Subsidiary to the extent of $29,253,066.30, an "open account" due from the Subsidiary in the amount of $27,154,584.03, and in the "segregated assets" amounting to $13,444,674.28 (R. 64). Its debts consisted of outstanding notes of the $30,000,000 note issue in the sum of $26,246,000 plus accrued interest as of October 24, 1931 in the amount of $656,150.00, besides a subordinated claim to its officers in excess of $10,000,000 (R. 64-65). When the

* In such event it was to act as "a trustee of an express trust" (R. 93).

second interest payment became due on November 1, 1931 on the $30,000,000 note issue, no funds were available and there was a threatened collapse of the entire Van Sweringen empire which would have also affected the $23,500,000 note of the Subsidiary in which the Trustee was interested as no funds were available to pay the interest which matured at the same time (R. 19-27).

A default in the $30,000,000 note issue would have enabled the Trustee to accelerate the entire issue, to take action for the application of the "segregated assets" and "assigned securities" in payment of the notes (R. 110-111), to obtain a deficiency for any balance against the Company, and to resort against its assets consisting primarily of the "open account" due from the Subsidiary in excess of $27,000,000. Such claim would have ranked equally with the claim of the Trustee and Morgan against the Subsidiary (R. 42). If the noteholders were aware of such facts they might have demanded such action from the Trustee by the joint action of 25% of the outstanding notes.

To avert the default (R. 28) and to prevent the consequences thereof the Trustee and Morgan (R. 43, 45) secretly worked out a plan whereby the Company would offer to the noteholders to use the cash available out of the "assigned securities", to pay one-half of the notes and to purchase the other half of the notes by the exchange for the common stock. The uncancelled notes so acquired were to be pledged as collateral in lieu of the common stock. By this scheme the noteholders would be deprived of their creditors' position for half of their debt and relegated to the position of common stockholders, and the Trustee and Morgan would have exchanged their role with the noteholders and substituted as creditors by the acquisition of the notes in exchange for the common stock which was pledged with them.

Thereby no action could be taken against the Subsidiary on the open account in excess of $27,000,000 as the only remaining creditors against it were the Trustee and Morgan and the other bankers who participated in the $23,500,000 loan. This agreement which was entered in writing with Morgan (R. 119) was never made public, nor was the fact that the Trustee actively participated in bringing about the accomplishment of the scheme (R. 43-44) ever revealed (R. 56-57).

The plan was carried out. The offer (R. 70) in the form prescribed by the Trustee and Morgan (R. 126) was made. The Trustee and Morgan exchanged the common stock for $13,887,000 uncancelled notes which were obtained as a result of the offer (R. 32). Plaintiff and the other noteholders received 50% in cash out of the "assigned securities" and for the balance of 50% they received the worthless stock (R. 29). The Trustee and Morgan realized out of the "assigned securities" some cash (R. 29-33) and received 12% from the collateral (R. 23) besides a deficiency decree against the Subsidiary in excess of $27,000,000 (See *Re Van Sweringen,* 111 F. (2) 378), and the claim of the noteholder for the deficiency was eliminated.

Opinion of the District Court. The opinion of the District Court in speaking of the "fiduciary relationship" between the Trustee and the plaintiff says (R. 134):

> "Both Morgan & Company and the Guaranty Trust Company, individually, were creditors of the Van Sweringen interests to the extent of $11,000,000 each, under loans made on October 30, 1930. In that situation, as Morgan & Company knew, the Guaranty Trust Company had both an individual fiduciary interest to serve. It thus owed its first duty to its trust, as Morgan & Company also knew."

The District Court, nevertheless, exonerated them from liability because: (1) the "segregated assets" and "assigned securities" were not a trust *res* (R. 136), and (2) Even if it was a trust *res* (R. 141) the proof did not show that the respondents received any part of these securities for their personal benefit.

The Report of the Senate Commission. After the rendition of the opinion by the court but before its final judgment there was received by counsel for the petitioner a printed report from the Senate Commission under Resolution 71, being Part 3 of Report No. 14. This Report was directly opposite to the view of the court pertaining to the motive of the Guaranty Trust Company and Morgan and illustrated the breach of faith and fraud as reported by the Senate Commission. Petitioners' counsel immediately forwarded the Report to the court asking it to reconsider its opinion and, if necessary, he would file a formal motion making the Report a part of the Record. The court refused to consider it and entered its final judgment. This matter was presented to the Circuit Court of Appeals by a formal motion for leave to file copies of the Report which the court denied and failed to consider on appeal (R. 153).

Opinion of Court of Appeals. The opinion of the Circuit Court of Appeals after disposing of the contention that the respondents were guilty of fraud considered the question whether there was a breach of trust. It said (R. 156):

> "Accepting the District Court's interpretation of the complaint as alleging a breach of trust as well as the fraud, we further agree that there was not, nor could there have been, any showing of a trust here. Actually the "Trust Indenture" securing the notes and naming the Guaranty Trust Company trustee

was no such thing. In place of the collateral usually deposited with a trustee, there were assets of the Van Sweringen Corporation which were to be kept segregated — but always in the possession of the company — and there was an agreement by which the Van Sweringen brothers were to deposit additional securities if necessary — but with the company, not the "Trustee." As we have said before, "A trust involves a specific subject matter of *res.*" * * * Here there is nothing upon which a trust can be founded."

The Court also said:

"There is, however, another reason why no action could be proved. For even assuming a fiduciary relationship, the plaintiff has suffered no loss or injury by the exchange. * * * at best the interest would have been defaulted and Guaranty Trust Company would have accelerated the principal. The noteholders would then have received just 50% of the principal plus a worthless stock interest in Cleveland Terminals Building Company plus a doubtful open account of the same company of $27,154,584.03. A glance at the balance sheet of that company shows that even this debt was practically, if not entirely, worthless since the assets of Cleveland consisted of real property that was not enough to satisfy the mortgages and securities pledged to more than their market value as collateral on a note issue. Thus it appears that the plaintiff failed to show, even *prima facie*, any injury resulting from her reliance upon the representations which accompanied the offer she accepted, and for this additional reason the judgment was right."

In the concurring opinion Judge Frank said:

"I concur, but solely on the ground stated in the last paragraph of the foregoing opinion. That is alone enough to sustain the decision. The other issues are less clear and I see no need to consider them."

It should be noted that while the District Court sustained the motion on the ground that the respondents did not benefit from the "offer" (R. 141) the Court of Appeals said that petitioner did not suffer any loss (R. 156, 157).*

The Petition for Rehearing. The petition for rehearing pointed out the existence of the trust relationship even if there were no trust *res* and the loss that the petitioner sustained was substantial and that any doubt must be resolved against the movants (R. 160-167). However, the court denied the rehearing.

QUESTIONS PRESENTED.

1. Whether a trust relationship was established between a noteholder and a Trustee which accepted its trust duties under a $30,000,000 note issue and which certified them as having been issued under its trust powers when they were sold to the public by a syndicate in which the Trustee's Subsidiary participated and which trust agreement vested the exclusive right of action as well as all discretionary duties in the Trustee, or, whether the Court of Appeals was correct in its conclusion that no trust relationship existed because there was no trust *res* in the possession of the Trustee.

2. Whether a summary judgment may be rendered for defendants on the ground that the benefits received by them as fiduciaries were of doubtful value and whether it was the duty of the Court of Appeals to construe Rule 56 so as to resolve the doubt against the movants, the respondents.

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* The opinion is in conflict with the authorities cited in Overfield v. Pennroad Corporation, 42 F. Supp. 586, 587, on the point that the rule of "undivided loyalty" does "not rest" upon the "narrow" ground of "injury" or "damage", but on the "broader foundation" of a wise "public policy".

REASONS FOR THE ALLOWANCE OF THE WRIT.

1. The decision of the Circuit Court of Appeals that no action for breach of trust was maintainable because no trust relationship was established between the petitioner and the Trustee, which accepted its trust duties and certified that it issued the notes pursuant to the terms and provisions contained in the trust instrument vesting the exclusive right of action as well as all discretionary duties in it, so far departs from the accepted general law relating to trusts as to call for the exercise of the Court's power of supervision.

2. The decision affirming the summary judgment against the Petitioner, the plaintiff, on the ground that the benefits received by the respondents from a breach of trust were of doubtful value is in conflict with the decision of the same Circuit in construing Rule 56 that every doubt must be resolved against the movant (*McElwain* v. *Wickmore Spencer Steel Co.*, 126 Fed. (2) 210). The decision is also in conflict with the opinion of the United States Court of Appeals for the District of Columbia (*Miller* v. *Miller,* 122 F. (2d) 209, 212) in the construction of Rule 56.

3. A summary judgment on the ground that the defendants did not benefit from their fraudulent acts or breach of trust may not be affirmed on the ground that the plaintiff did not prove even *prima facie* that she sustained any loss and it was the duty of the court to construe Rule 56 as to resolve every doubt in favor of the petitioner and against the movants. Because of the improper construction of the new federal rules the writ should be issued.

4. The tendency of the courts to look beyond corporate forms to the purpose of the corporate acts and to the persons and human beings who moved and operated in the name of a legal entity for their selfish interest, was entirely overlooked. The principle of fiduciary relationship and obligations resulting from the acts of the parties irrespective of the legal forms, and the cardinal rule that no one may serve two masters, based on the moral obligation to refrain from being placed in a position which would excite a conflict between self-interest and integrity of duty, was brushed aside by a technical construction of the instrument which the Trustee executed and on which faith the public invested $30,000,000. To say that a trust instrument of this nature is "nothing" and thereby exempt the Trustee from liability for breach of trust is not in conformity with sound, equitable principles, and it is contrary to public policy. Therefore, the decision deserves a review by this Court.

5. The question whether an official report of a Congressional Committee may be considered by a court without formally introducing it in evidence in connection with a motion for a summary judgment by defendants when the Report throws light on the subject whether the defendants were motivated by honest intentions and whether they defrauded the plaintiff and violated their trust duties is a question that has not yet been squarely passed on by this court and is of extreme importance in the administration of justice and federal procedure.

PRAYER FOR RELIEF.

Wherefore, the above petitioner prays the allowance of a writ of *certiorari* to the United States Circuit Court of Appeals for the Second Circuit, to the end that its judgment may be reviewed and decided by this Court and reversed with proper directions.

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